

AMENDED IN SENATE MAY 25, 2005

AMENDED IN SENATE APRIL 21, 2005

**SENATE BILL**

**No. 747**

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**Introduced by Senator Machado**

February 22, 2005

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An act to amend Sections 5100 and 22250 of, and to add Section 6106.3 to, the Business and Professions Code, to amend Section 19178 of, and to add Sections 19169.1, 19169.3, 19177.1, 19177.3, and 19178.5 to, the Revenue and Taxation Code, relating to taxation.

LEGISLATIVE COUNSEL'S DIGEST

SB 747, as amended, Machado. Tax professionals: discipline.

Existing law regulates the practice of law and the practice of accounting in this state. Existing law also requires that a penalty be imposed against individuals who promote abusive tax shelters or who aid and abet in the understatement of tax liabilities.

This bill would make the imposition of penalties for promoting abusive tax shelters or aiding and abetting the understatement of tax liabilities grounds for the revocation or suspension of the license, permit, or certificate to practice of an attorney, accounting firm, person associated with an accounting firm, tax preparer, or other person. The bill would prohibit tax preparers assessed a final penalty for those activities from preparing taxes for a period of 5 years. The bill would impose specified penalties and prohibitions against other individuals and taxpayers who engage in specified activities related to abusive tax shelters or aiding and abetting the understatement of tax liabilities and would prohibit specified individuals from receiving compensation for tax services when the compensation is determined by reference to the amount of tax shown on a return. The bill would require the Franchise Tax Board to notify specified state entities when

a person is assessed a penalty for violating existing law ~~and would require the State Bar to undertake a specified study of the activities of certain attorneys and report the State Bar's findings to the Legislature by a specified date.~~ The bill would also increase the penalties for violations of existing law.

Vote: majority. Appropriation: no. Fiscal committee: yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

1 SECTION 1. Section 5100 of the Business and Professions  
2 Code is amended to read:

3 5100. After notice and hearing the board may revoke,  
4 suspend, or refuse to renew any permit or certificate granted  
5 under Article 4 (commencing with Section 5070) and Article 5  
6 (commencing with Section 5080), or may censure the holder of  
7 that permit or certificate for unprofessional conduct that includes,  
8 but is not limited to, one or any combination of the following  
9 causes:

10 (a) Conviction of any crime substantially related to the  
11 qualifications, functions and duties of a certified public  
12 accountant or a public accountant.

13 (b) A violation of Section 478, 498, or 499 dealing with false  
14 statements or omissions in the application for a license, in  
15 obtaining a certificate as a certified public accountant, in  
16 obtaining registration under this chapter, or in obtaining a permit  
17 to practice public accountancy under this chapter.

18 (c) Dishonesty, fraud, gross negligence, or repeated negligent  
19 acts committed in the same or different engagements, for the  
20 same or different clients, or any combination of engagements or  
21 clients, each resulting in a violation of applicable professional  
22 standards that indicate a lack of competency in the practice of  
23 public accountancy or in the performance of the bookkeeping  
24 operations described in Section 5052.

25 (d) Cancellation, revocation, or suspension of a certificate or  
26 other authority to practice as a certified public accountant or a  
27 public accountant, refusal to renew the certificate or other  
28 authority to practice as a certified public accountant or a public  
29 accountant, or any other discipline by any other state or foreign  
30 country.

1 (e) Violation of Section 5097.

2 (f) Violation of Section 5120.

3 (g) Willful violation of this chapter or any rule or regulation  
4 promulgated by the board under the authority granted under this  
5 chapter.

6 (h) Suspension or revocation of the right to practice before any  
7 governmental body or agency.

8 (i) Fiscal dishonesty or breach of fiduciary responsibility of  
9 any kind.

10 (j) Knowing preparation, publication, or dissemination of  
11 false, fraudulent, or materially misleading financial statements,  
12 reports, or information.

13 (k) Embezzlement, theft, misappropriation of funds or  
14 property, or obtaining money, property, or other valuable  
15 consideration by fraudulent means or false pretenses.

16 (l) The imposition of any discipline, penalty, or sanction on a  
17 registered public accounting firm or any associated person of  
18 such firm, or both, or on any other holder of a permit, certificate,  
19 license, or other authority to practice in this state, by the Public  
20 Company Accounting Oversight Board or the United States  
21 Securities and Exchange Commission, or their designees under  
22 the Sarbanes-Oxley Act of 2002 or other federal legislation.

23 (m) Unlawfully engaging in the practice of public accountancy  
24 in another state.

25 (n) (1) The imposition, by the Franchise Tax Board, of the  
26 penalty pursuant to Section 19177 or 19178 of the Revenue and  
27 Taxation Code on a registered public accounting firm, any person  
28 associated with a public accounting firm, or any other holder of a  
29 permit, certificate, license, or other authority to practice in this  
30 state.

31 (2) The Legislature finds and declares that the promotion of,  
32 and investment in, abusive tax shelters and the aiding or abetting  
33 taxpayers in understating their taxes, constitutes serious problems  
34 that are undermining the fundamental integrity of the  
35 self-assessed tax system. ~~The Legislature further finds and~~  
36 ~~declares that it is in the public interest to revoke, suspend, or~~  
37 ~~refuse to renew the permits, certificates, and licenses of any~~  
38 ~~registered public accounting firm, persons associated with a~~  
39 ~~registered public accounting firm, and any other holder of a~~  
40 ~~permit, certificate, or license to practice in this state who~~

~~promotes abusive tax shelters or who aids or abets taxpayers in understating their income and franchise tax liabilities.~~

SEC. 2. Section 6106.3 is added to the Business and Professions Code, to read:

6106.3. (a) It shall constitute cause for disbarment or suspension for an attorney to engage in conduct subject to penalty pursuant to Section 19177 or 19178 of the Revenue and Taxation Code.

(b) The Legislature finds and declares that the promotion of, and investment in, abusive tax shelters and the aiding or abetting taxpayers in understating their taxes, constitutes serious problems that are undermining the fundamental integrity of the self-assessed tax system. ~~The Legislature further finds and declares that it is in the public interest to revoke or suspend the license of any attorney to practice in this state who promotes abusive tax shelters or who aids or abets taxpayers in understating their income and franchise tax liabilities.~~

SEC. 3. Section 22250 of the Business and Professions Code is amended to read:

22250. (a) A tax preparer shall maintain a bond issued by a surety company admitted to do business in this state for each individual preparing tax returns for another person. The principal sum of the bond shall be five thousand dollars (\$5,000). A tax preparer subject to this section shall provide to the surety company proof that the individual is at least 18 years of age before a surety bond may be issued.

(b) The bond required by this section shall be in favor of, and payable to, the people of the State of California and shall be for the benefit of any person or persons damaged by any fraud, dishonesty, misstatement, misrepresentation, deceit, or any unlawful acts or omissions by the tax preparer, or the tax preparers employed or associated with it to provide tax preparation services.

(c) The tax preparer filing the bond shall identify all tax preparers employed or associated with the tax preparer and shall provide for each employee or associate the evidence required by subdivision (a) to the surety company. A tax preparer employed or associated with a tax preparer shall be covered by the bond of the tax preparer with which he or she is employed or associated. However, in no event shall the total bond required for any single

1 tax preparer and the tax preparers employed or associated with it  
2 be required to exceed one hundred twenty-five thousand dollars  
3 (\$125,000). The aggregate liability of the surety to any and all  
4 persons regardless of the number of claims against the bond or  
5 the number of years the bond remains in force shall not exceed  
6 five thousand dollars (\$5,000) for any one tax preparer. Any  
7 revision of the bond amount shall not be cumulative. The liability  
8 of the surety on the bond shall not include payment of any civil  
9 penalties, fines, attorneys' fees, or any other cost provided by  
10 statute or regulation.

11 (d) The tax preparer shall file an amendment to the bond  
12 within 30 days of a change in information contained in the bond,  
13 including a change in the tax preparers employed or associated  
14 with the tax preparer.

15 (e) (1) A tax preparer may not conduct business without  
16 having a current surety bond in the amount prescribed by this  
17 section.

18 (2) Thirty days prior to the cancellation or termination of any  
19 surety bond required by this section, the surety shall send a  
20 written notice of that cancellation or termination to the tax  
21 preparer and the California Tax Education Council, identifying  
22 the bond and the date of cancellation or termination.

23 (3) If a tax preparer fails to obtain a new bond by the effective  
24 date of the cancellation or termination of the former bond, the tax  
25 preparer shall cease to conduct business until that time as a new  
26 surety bond is obtained.

27 (f) Notwithstanding Section 995.710 of the Code of Civil  
28 Procedure, a tax preparer may not make a deposit in lieu of bond.

29 (g) A tax preparer shall furnish evidence of the bond required  
30 by this section upon the request of any state, federal agency or  
31 any law enforcement agency or the California Tax Education  
32 Council.

33 (h) A tax preparer for which a penalty pursuant to Section  
34 19177 or 19178 of the Revenue and Taxation Code has been  
35 assessed and finalized in accordance with subdivision (c) of  
36 Section 19180 of the Revenue and Taxation Code is prohibited  
37 from conducting the business subject to regulation pursuant to  
38 this chapter for five years from the date the penalty is finalized.

39 SEC. 4. Section 19169.1 is added to the Revenue and  
40 Taxation Code, to read:

1 19169.1. (a) Any person for which a penalty pursuant to  
2 Section 19177 or 19178 ~~of the Revenue and Taxation Code~~ has  
3 been assessed and finalized in accordance with subdivision (c) of  
4 Section 19180 ~~of the Revenue and Taxation Code~~ is subject to all  
5 of the following:

6 (1) Suspension or prohibition from preparing tax returns for  
7 compensation or employing, or arranging for, any person to  
8 prepare tax returns for compensation.

9 (2) Suspension or prohibition from representing a person,  
10 other than himself or herself, before the Franchise Tax Board or  
11 State Board of Equalization in a matter arising under this part,  
12 Part 10, or Part 11.

13 (b) The Franchise Tax Board shall prescribe those regulations  
14 necessary to implement the purposes of this section.

15 (c) For purposes of this section, “person” includes related  
16 taxpayers as defined in Section 267 of the Internal Revenue  
17 Code.

18 SEC. 5. Section 19169.3 is added to the Revenue and  
19 Taxation Code, to read:

20 19169.3. (a) A person who performs any service related to  
21 financial information reflected on a return filed pursuant to this  
22 part, Part 10, or Part 11 may not receive compensation for that  
23 service, or portion thereof, that is determined or computed,  
24 directly or indirectly, by reference to the amount of tax shown on  
25 a return prepared by the person.

26 (b) For purposes of this section, “person” includes related  
27 taxpayers as defined in Section 267 of the Internal Revenue  
28 Code.

29 SEC. 6. Section 19177.1 is added to the Revenue and  
30 Taxation Code, to read:

31 19177.1. (a) A person or person who employs an individual  
32 who offers for sale or promotes the sale of an abusive tax shelter  
33 or listed transaction to a taxpayer may not prepare, for  
34 compensation, a tax return for that taxpayer.

35 (b) For purposes of this section, “person” includes related  
36 taxpayers as defined in Section 267 of the Internal Revenue  
37 Code.

38 (c) For purposes of this section, “prepare for compensation”  
39 shall include the activities described in subdivision (b) of Section  
40 19169.

SEC. 7. Section 19177.3 is added to the Revenue and Taxation Code, to read:

19177.3. Any person who fails to comply with Sections 19169.3 or 19177.1 is subject to a penalty equal to the greater of ten thousand dollars (\$10,000) or 75 percent of the compensation the person received to prepare the tax return.

SEC. 8. Section 19178 of the Revenue and Taxation Code is amended to read:

19178. (a) A penalty shall be imposed for aiding and abetting understatement of tax liability. The penalty shall be determined in accordance with Section 6701 of the Internal Revenue Code, unless otherwise provided.

(b) For purposes of this section:

(1) The phrase “or should have known” shall replace the phrase “or has reason to believe” in Section 6701(a)(2) of the Internal Revenue Code.

(2) The phrase “should have known” shall replace the word “knows” in Section 6701(a)(3) of the Internal Revenue Code.

(3) Section 6701(b)(1) of the Internal Revenue Code shall be modified by substituting “\$25,000” for “\$1,000.”

(4) Section 6701(b)(2) of the Internal Revenue Code shall be modified by substituting “\$100,000” for “\$1,000.”

SEC. 9. Section 19178.5 is added to the Revenue and Taxation Code, to read:

19178.5. The Franchise Tax Board shall notify any and all appropriate state departments, agencies, and other similar organizations overseeing the person against whom a penalty is assessed pursuant to Section 19177 or 19178.

~~SEC. 10. The State Bar shall conduct a study to determine whether attorneys employed by accounting firms are giving legal advice to the accounting firm’s clients that is to the possible detriment of the client. The State Bar shall report its findings to the Legislature within one year of the effective date of this act.~~